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Letter Ruling 95-4: Massachusetts NOL Carryover Survives a Statutory Merger that Qualifies as an 'F' Reorganization

March 31, 1995

Issue

You request a ruling on behalf of ***** (hereinafter “MassCorp”), addressing the issue of whether Massachusetts net operating loss carryover survives a statutory merger that also qualifies as an F reorganization.

Facts

MassCorp is incorporated under the laws of the Commonwealth of Massachusetts and has its principal offices located in ***** Massachusetts. MassCorp is engaged primarily in the research and development, manufacturing and marketing of medical diagnostic products using a proprietary biosensor technology.

MassCorp is currently considering changing its state of incorporation from Massachusetts to Delaware. The reorganization will be effected as follows: 1) MassCorp will form a new corporation under the laws of the state of Delaware (“DelCorp”); 2) each share of the outstanding stock of MassCorp will be converted into an equivalent share of stock of DelCorp. Following the conversion, MassCorp will terminate its corporate existence. It is intended that the conversion will qualify for federal purposes as a tax free reorganization under I.R.C. § 368(a)(1)(F) (1986 as amended) (hereinafter an “F” reorganization).

Subsequent to such reincorporation, DelCorp will continue the identical business carried on by MassCorp prior to the change in its state of incorporation and will have the identical shareholder group that MassCorp had prior to such change. The only difference in the activities, operations and corporate structure of DelCorp will be its state of incorporation.

MassCorp wishes to reincorporate in another state for valid business reasons and not to achieve any state or federal tax savings. Subsequent to such reincorporation, MassCorp will continue to operate its corporate headquarters and manufacturing facility in ***** Massachusetts, and as such, will continue to file a Massachusetts corporate excise tax return. Since the time of its incorporation, MassCorp’s operational activities have generated losses. As of its most recent tax year, MassCorp

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had approximately 50 million dollars of net operating loss available for carryforward.

Discussion of Law

The Massachusetts net operating loss was enacted in 1973 and was available to new corporations in their first five years of business. G.L. c. 63, § 30.5(b). In 1989, the Massachusetts net operating loss was made available to all corporations, not just new corporations, subject to certain phase-in limitations. M.G.L. c. 63, § 30.5(b) & (c), permits carryover of Massachusetts net operating losses subject to certain restrictions and limitations. The Net Operating Loss Deductions and Carryover Regulation, 830 CMR 63.30.2(11), limits net operating loss carryover where there is a merger of two or more corporations. However, the regulation does not provide rules for statutory mergers involving only one corporation.

To determine whether net operating loss carryover survives a statutory merger that qualifies as an F reorganization, we look to the purpose behind carryover provisions. Carryover provisions allow a departure from the general system of a strict annual accounting to bring stability to the tax burden of a business with fluctuating years of profit and loss. Newmarket Manufacturing Co. v. United States, 233 F.2d 493, 496 (1956) citing H.R. Rep. No. 855, 67th Cong., 1st Sess. 9-10 (1939). Restricting the use of net operating loss carryover to the taxpaying entity that incurred the loss is a formalistic approach that has been criticized and abandoned at the federal level. See generally Libson Shops, Inc. v. Koehler, 353 U.S. 382 (1957). "The transferee in a statutory merger should be deemed to be continuing in itself the corporate life of the now-defunct component. It follows from this conceptual identity that the two corporate entities are to be treated for a substantive purpose in the income tax as the same taxpayer." Newmarket, 233 F.2d at 498. These concepts are now expressly incorporated in the Internal Revenue Code, which provides that an F reorganization, defined as a mere change in identity, form or place of organization, of one corporation, [\[1\]](#) will not cause a corporation to lose its net operating loss carryover. I.R.C. § 381(b).

Although the facts considered in this ruling involve a statutory merger of two corporate entities, one of these corporations will be created solely for purposes of the transaction. After the reincorporation, the identical business carried on by the terminated corporation will continue in the successor. The successor will have the same assets and the identical shareholder group that the terminated corporation had prior to the merger. The only change in the activities, operation and structure of the successor corporation will be its state of incorporation. Thus, there is only one ongoing business enterprise and this single enterprise continues essentially unchanged through the proposed reorganization. The Net Operating Loss Deductions and Carryover Regulation, 830 CMR 63.30.2, limits net operating loss carryover in mergers involving two or more corporations. Net operating loss carryover is not precluded in an F reorganization, which by definition involves only one corporation, even where the F reorganization takes the form of a statutory merger for corporate law purposes.

Conclusion

Massachusetts net operating loss carryover survives a statutory merger if the transaction also qualifies as an F reorganization under I.R.C § 368(a)(1)(F). The Massachusetts net operating loss carryover will be preserved to the extent that it could have been utilized by the transferor corporation had there been no merger. Accordingly, DelCorp may deduct the net operating loss carryover to the extent it would have been available to MassCorp had there been no merger.

Very truly yours,

/s/Mitchell Adams

Mitchell Adams
Commissioner of Revenue

MA:HMP:dmm

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[\[1\]](#) I.R.C. § 368(a)(1)(F). Revenue Ruling 57-276, 1957-1 C.B. 126, provides that a statutory merger may also qualify as an F reorganization.